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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938

No. 304

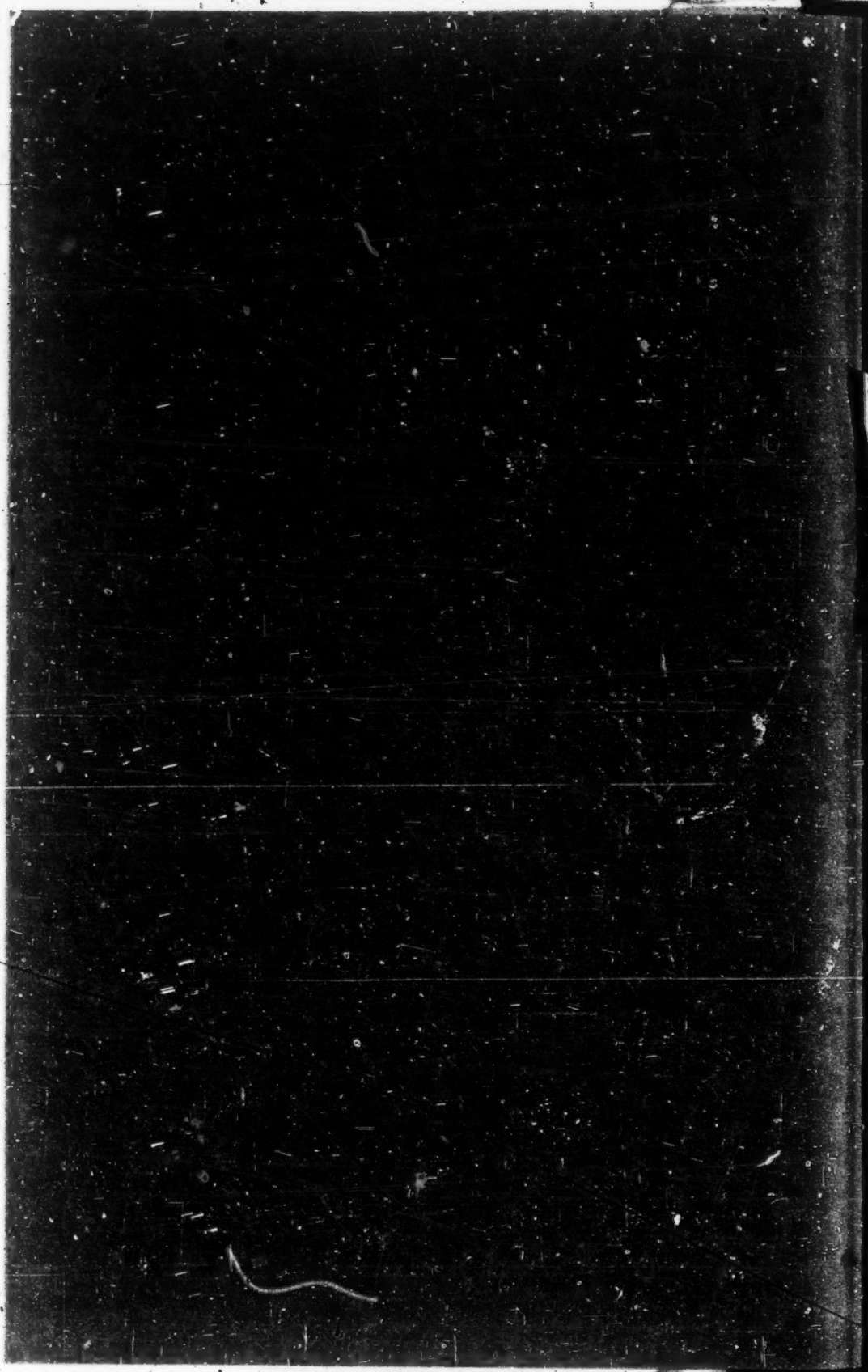
GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

CHESTER N. WEAVER COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR CERTIORARI FILED AUGUST 26, 1938
CERTIORARI GRANTED OCTOBER 10, 1938



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104469—38

APPEARANCES:

For Taxpayer:

ADOLPHUS E. GRAUPNER,
ARTHUR E. COOLEY, Esq.

For Comm'r:

O. W. SWECKER, Esq.
Transferred to Mr. Turner 11/20/36.

Docket No. 82865

CHESTER N. WEAVER CO. a corporation.
Petitioner.

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES.

1936

Feb. 4—Petition received and filed. Taxpayer notified. (Fee paid).

Feb. 5—Copy of petition served on General Counsel.

Mar. 24—Answer filed by General Counsel.

Mar. 26—Copy of answer served on taxpayer.

May 8—Hearing set week of 7-6-36 at San Francisco, Calif.

July 6—Hearing had before Mr. C. P. Smith, Div. 5, on the merits. On Counsel's motion 82865, 82870 and 82871 consolidated. Stipulation as to facts filed. Pet's brief due Aug. 6, 1936. Respondent's 9/7/36. Reply due Oct. 7, 1936.

July 27—Brief filed by taxpayer. 7/28/36 copy served.

July 31—Transcript of hearing July 6, 1936, filed.

Sept. 18—Motion for leave to Sept. 19, 1936 to file brief, filed by General Counsel. Brief lodged. 9/18/36 Granted.

Oct. 19—Reply brief filed by taxpayer. 10/19/36 copy served.

1937

Feb. 17—Findings of fact and opinion rendered, Bolon B. Turner, Div. 8. Decision will be entered under Rule 50.

Feb. 27—Motion for decision under rule 50 filed by General Counsel.

Mar. 3—Hearing set March 24, 1937 on settlement.

Mar. 12—Consent to settlement filed by taxpayer.

Mar. 20—Decision entered, Bolon B. Turner, Div. 8.

Apr. 20—Supersedeas bond in the amount of $8,646.96 approved and ordered filed.

Apr. 20—Petition for review by United States Circuit Court of Appeals, Ninth Circuit, with assignments of error filed by taxpayer. Affidavit service of petition for review filed.

Apr. 21—Proof of service filed by taxpayer.
May 24—Praecipe, filed by taxpayer.
May 24—Affidavit of service of praecipe filed.
May 24—Order from Circuit Court of Appeals, 9th Circuit that procedure as stipulated by both parties be adopted—further proceedings in accordance therewith—filed. [1*]

United States Board of Tax Appeals

Docket No. 82865

CHESTER N. WEAVER CO., a corporation,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION.

Without waiver of right to challenge the constitutionality of any part of any Revenue Act involved in this proceeding or any act of the Commissioner of Internal Revenue or his subordinates or to object to the jurisdiction of this Board, the above named petitioner hereby petitions for a redetermination of the alleged deficiency set forth by the Commissioner of Internal Revenue in his purported notice of deficiency (IT:AR:E-4, GCD-

*Page numbering appearing at the foot of page of original certified Transcript of Record.

90D) dated December 30, 1935, and as a basis of this proceeding alleges as follows:

1. The petitioner is a corporation duly organized and existing under the laws of the State of California with its principal place of business at 516 Sutter Street, City and County of San Francisco, State of California.

2. The purported notice of deficiency upon which this petition is based (a copy of which is hereunto attached and marked Exhibit A) was apparently mailed to the petitioner on December [2] 30, 1930.

3. The asserted deficiency in tax here in controversy is for alleged income taxes for the calendar year 1933 and, as asserted in said purported deficiency notice, in the amount of not more than $4,323.48.

4. The alleged determination of tax set forth in said purported notice of deficiency is erroneous in each and every of the following particulars assigned as errors:

(a) The Commissioner erred in determining and asserting any amount as a deficiency in income tax against petitioner for the calendar taxable year 1933.

(b) The Commissioner erred in increasing in any way the net income reported by petitioner in its income tax return for the calendar taxable year 1933 and in making any reductions from the net income reported by petitioner in said return for said year.

(c) The Commissioner erred in treating as taxable income and disallowing items of reserve in the amount of $3,328.49 which petitioner had set up and maintained on its books of account as a regular and necessary part of its accounting system.

(d) The Commissioner erred in disallowing the amount of $86,859.75 deducted by petitioner from gross income reported in its income tax return for the taxable year herein involved as a loss sustained *though* the dissolution of the Jeff R. Townsend Co., Inc., a corporation.

(e) The Commissioner erred in disallowing the amount of $6,163.04 deducted by petitioner from income reported in its income tax return for the taxable year herein involved as depreciation on [3] certain buildings, office furniture and equipment, machinery and machine shop equipment, and automobiles employed and used by petitioner in the conduct of its business during said taxable year.

(f) The Commissioner erred in disallowing the amount of $56.00 deducted by petitioner from income reported in its income tax return for the taxable year herein involved as depreciation on a fence located on business property in Oakland, California, and owned by petitioner.

5. The facts upon which the petitioner relies as a basis for this proceeding are as follows:

(a)—During the taxable year 1933 herein involved petitioner was engaged in the business of buying, selling, repairing and servicing automobiles, in making investments in stocks and securi-

ties of other corporations and in obligations of the United States and of States and political subdivisions thereof, and in maintaining and operating real property.

(b)—That petitioner had established in its books of account the reserve method of treating various items of expected and anticipated losses and expenses and particularly had established and set up for the taxable year involved a reserve for repossession of automobiles sold on the installment basis in the amount of $3,012.60 and a reserve for insurance in the amount of $315.89. In its income tax return for the taxable year involved the petitioner deducted the amounts of said reserves from its gross income. The respondent denied the deductibility of said items of reserve and added the sum of $3,328.49, representing the amount of said reserves, to petitioner's txable net income.

(c)—On or about August 9, 1932, petitioner purchased for [4] cash one thousand shares of the preferred stock of the Jeff R. Townsend Co., Inc., having a par value of one hundred dollars per share, and paid therefor the amount of $100,000. Said Jeff R. Townsend Co., Inc. was engaged in the business of buying, selling, repairing and servicing automobiles. In September, 1933, the Jeff R. Townsend Co., Inc. was liquidated and petitioner received from said corporation, as a complete liquidating dividend on dissolution thereof, the amount of $13,140.25 and thereby sustained a loss of $86,859.75 on its investment of $100,000. That petitioner

deducted said amount of $86,859.75 from its gross income reported in its return for the taxable year involved as a loss sustained in the conduct of its business. That respondent disallowed said loss as a deductible item and added the amount thereof to petitioner's taxable net income for said taxable year.

(d)—Petitioner as the owner of various depreciable properties claimed as a deduction for depreciation in its income tax return for the taxable year involved the sum of $20,830.42, which sum was computed at the rates of depreciation returned by petitioner and allowed by respondent for previous taxable years and was reasonable in rate and amount in relation to the age and character of the properties and the purposes for which they were used. That respondent reduced the rates of depreciation claimed and returned by petitioner for the taxable year and disallowed the amount of $6,497.75 as asserted excessive depreciation for said year and added said amount to petitioner's taxable net income for said year.

(e)—Petitioner's income and excess profits tax return for the taxable year herein involved disclosed a net loss of $64,403.79 and no tax due or payable. By his arbitrary and illegal disallowance [5] of proper deductions and the addition of the sum thereof to petitioner's returned net income, respondent has illegally and erroneously increased petitioner's taxable net income in the sum of $96,407.28 for the taxable year involved and has there-

on illegally and erroneously determined an alleged deficiency in tax against your petitioner for said year in the amount of $4,323.48.

Wherefore, the petitioner prays that this Board may hear the proceeding and determine that there is no deficiency in tax or additional tax due and owing respondent or any other officer or person from petitioner for the taxable year involved and that it grant petitioner such other and further relief as may be meet.

ADOLPHUS E. GRAUPNER
ARTHUR E. COOLEY
Attorneys for Petitioner
1110 Balfour Building
San Francisco, California [6]

State of California
City and County of San Francisco—ss.

Chester N. Weaver, being duly sworn, says that he is the president of the Chester N. Weaver Co., a corporation, the petitioner herein, and that he is duly authorized to verify the foregoing petition; that he has read the foregoing petition and is familiar with the statements contained therein, and that the facts stated are true, except as to those facts stated on information and belief, and those facts he believes to be true.

CHESTER N. WEAVER

Subscribed and sworn to before me this 29th day of January, 1936.

[Seal] DOROTHY H. McLENNAN,
Notary Public in and for the City and County of San Francisco, State of California. My commission expires December 24, 1938. [7]

EXHIBIT A

Dec. 30, 1935.

IT:AN:E-4
GCD-90D
Chester N. Weaver Co.,
516 Sutter Street,
San Francisco, California.

Sirs:

You are advised that the determination of your income tax liability for the taxable year 1933 discloses a deficiency of $4,323.48 as shown in the statement attached.

In accordance with section 272 (a) of the Revenue Act of 1932, as amended by section 501 of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Wash-

ington, D. C., for the attention of IT:C:P-7. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,

Commissioner.

By (Signed) CHAS. T. RUSSELL

Deputy Commissioner.

Enclosures:

Statement

Form 870

GCD/TVW-1. [8]

STATEMENT

IT:AR:E-4

GCD-90D

In re Chester N. Weaver Co.,
516 Sutter Street,
San Francisco, California.

Income Tax Liability

Year—1933.

Income Tax Liability—$4,323.48.

Income Tax Assessed—None.

Deficiency—$4,323.48.

The deficiency shown herein is based upon the report prepared by Internal Revenue Agent D. W.

Johnson, dated April 16, 1935, a copy of which was transmitted to you May 8, 1935, and as the result of a conference held in the office of the internal revenue agent in charge, San Francisco, California, September 6, 1935.

Net income shown on return (loss)		($64,403.79)
Add:		
1. Unallowable reserve	$ 3,328.49	
2. Loss on Townsend Company stock not deductible	86,859.75	
3. Excess depreciation	.6,163.04	
4. Depreciation on fence reversed	56.00	
	$96,407.28	
Deduct:		
5. Capital stock tax accrued December 31, 1933	560.00	95,847.28
Adjusted net income		$31,443.49
Income tax at 13¾%		$ 4,323.48
Previously assessed, original, account #856078		None
Deficiency		$ 4,323.48

[9]

Explanation of Changes

1. The following are considered unallowable reserves not deductible from income:

Reserve for repossession	$3,012.60
Reserve for insurance	315.89
Total	$3,328.49

These reserves relate to automobile sold on term contracts which you carry and do not discount. At the time of sale, an estimate of the probable loss

in event of repossession, etc., is credited to the "Reserve for Repossession" and the amount added to the contract sales price in excess of the cash sales price for insurance carried by you is credited to the "Reserve for Insurance."

Since you report income on an accrual basis, it is held that the credits to the above-named "Reserves" represent taxable income, the losses or other charges thereto being deductible. As you did not begin the auto sales business until April, 1933, the "reserves" in question were all set up within the taxable year under consideration. Therefore, the net credit balance of $3,328.49 is adjusted to taxable income.

2. The records of this office show that in 1931 the Jeff R. Townsend Company was organized by Mr. Weaver and other individuals for the purpose of taking over the automobile business of your company; that a portion of your business was sold to the Townsend Company for cash. Your corporation held none of the common or voting stock of the Jeff R. Townsend Company, but on August 9, 1932, purchased 1,000 shares of its preferred stock for $100,000.00. On March 20, 1933 a resolution was passed by your company to sell the automobile stock and business of the Townsend Company to your company, and on March 28, 1933 a resolution was passed to take the necessary steps to dissolve the Jeff R. Townsend Company. This was finally effected by a sale on September 15, 1933 of the remaining assets, chiefly cash and minor accounts.

The liquidation took place on September 16, 1933 and you received the sum of $13,140.25 as a liquidating dividend, resulting in a loss in the amount of $86,859.75. A deduction in this amount was taken on your return, which was disallowed by the revenue agent in his report covering the examination thereof. [10]

The disallowance was made upon the authority of section 23(r) of the Revenue Act of 1932 for the reason that you had no gain from sales or exchanges of assets held less than two years, and the loss sustained in connection with the stock is held to be from an exchange of stock held less than two years. Section 115(c) of the Revenue Act of 1932 is given as authority for holding that a transaction involving the liquidation of a corporation is to be treated as an exchange.

Section 23(r) of the Revenue Act of 1932 limits the deduction for stock losses and provides as follows:

> "Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations)."

Section 111(c) of the Revenue Act of 1932 which refers to recognition of gain or loss, contains no reference to section 23(r) and contains provisions

relative to sales and exchanges which are similar to those found in section 115(c) relative to distributions in liquidation. See below.

> "Recognition of gain or loss—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purpose of this title, shall be determined under the provisions of section 112."

In transactions coming under the provisions of section 115(c) or 111(c) the deduction for losses is allowable only as provided in section 23(e) which relates to the deduction to be allowed to an individual in computing net income. This section provides for the allowance of certain losses, subject to the limitation provided in section 23(r).

The report of the examining agent has been sustained relative to the disallowance of the loss in the amount of $86,595.75 arising because of the liquidation of the Jeff R. Townsend Company upon the grounds that a transaction involving a distribution in liquidation is to be treated as an exchange and that the limitation set forth in section 23(r) of the Revenue Act of 1932 applies to such transactions.

[11]

3. For details of depreciation, see copy of exhibit attached.

4. Depreciation on fence not deducted on the books restored to income.

5. Capital stock tax not accrued at December 31, 1933 is deductible on the basis of the following computation:

Declared value of capital stock January 1, 1932			$800,990.00
Surplus per books December 31, 1932		$489,000.29	
Surplus December 31, 1933		234,959.34	
Decrease in 1933		$254,040.95	
Less:			
Adjustments increasing surplus per schedule #1 herein:			
Unallowable reserves	$6,994.85		
Excessive depreciation	6,497.75	13,492.60	240,548.35
Value capital stock December 31, 1933			$560,441.65
Capital stock tax at $1.00 for each $1,000.00			560.00

In case you agree to the entire amount of the deficiency, please fill in the amount of $4,323.49 on the enclosed form 870 (Waiver of Restrictions) and forward it, properly executed, to the Commissioner of Internal Revenue, Washington, D. C. However, if you do not acquiesce in all of the adjustments making up the deficiency indicated, but would like to stop the accumulation of interest on that part of the deficiency resulting from adjustments to which you agree, please fill out the form 870 inserting therein the amount you desire to have assessed at once. In the event that you agree to only a part of the deficiency indicated, the execution of the form for the agreed portion of the deficiency will not deprive you of your right to petition the United States Board of Tax Appeals for a redetermination of the income tax liability for the year or years to which it relates.

A copy of this letter, together with a copy of the statement, has been mailed to your representative.

Mr. Arthur E. Cooley, 206 Sansome Street, San Francisco, California, in accordance with the authority conferred upon him in the power of attorney executed by you and on file with the Bureau. [12]

Exhibit "D"
Depreciation Schedule

Item	Cost Basis for Depreciation	Estimated Life (Years)	
S. F. Building	$335,321.60	25	$ 9,102.79
Oakland Building	150,620.41	33⅓	4,518.61
Oakland fence	560.00	10	56.00
Office furniture and equipment S. F.	2,420.00		208.00
Office furniture and equipment Oakland	3,999.86		283.69
Machinery and equipment Oakland	3,786.78		280.45
Service cars Oakland	510.00		81.84
S. F. house car	695.66		80.00
Total depreciation allowable			$14,611.38
Total depreciation per books			20,774.42
Excessive depreciation disallowed			$ 6,163.04
Total cost to January 1, 1933			$174,071.29
Less:			
Depreciation allowed to January 1, 1933			23,450.88
Remaining cost January 1, 1933			$150,620.41
Allowable depreciation on basis of an estimated life of approximately 33⅓ years from January 1, 1933 3% of $150,620.41 or			$ 4,518.61
Depreciation allowed in original report			4,183.90
Additional depreciation allowable			$ 334.71

GCD/TVW-1

[Endorsed]: U.S.B.T.A. Filed Feb. 4, 1936. [13]

[Title of Court and Cause.]

ANSWER

Comes now the Commissioner of Internal Revenue, by his attorney, Herman Oliphant, General Counsel for the Department of the Treasury, and for answer to the petition filed by the above-named petitioner admits and denies as follows, to-wit:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Denies that the notice of deficiency upon which the petition is based was mailed to petitioner on December 30, 1930, as alleged in paragraph 2 of the petition. Alleges that the said notice of deficiency was mailed to petitioner on December 30, 1935.

3. Admits that the amount in controversy is for income taxes for the calendar year 1933. Denies the remaining allegations of paragraph 3 of the petition.

4(a) to (f), inc. Denies that the Commissioner erred as alleged in paragraphs 4(a) to (f), inclusive, of the petition.

5(a). Admits that during the taxable year 1933 herein involved petitioner was engaged in the business of buying, selling, repairing and [14] servicing automobiles. Denies the remaining allegations contained in paragraph 5(a) of the petition.

(b). Admits that in its income tax return for the taxable year involved the petitioner deducted the sum of $3,328.49 as so-called reserves from its gross income and that the respondent disallowed the

deduction of the said amount and added the said sum of $3,328.49 to petitioner's taxable net income. Denies the remaining allegations contained in paragraph 5(b) of the petition.

(c). Admits that petitioner deducted the amount of $86,859.75 from its gross income reported in its return for the taxable year involved as a loss alleged to have been sustained on the liquidation of the Jeff R. Townsend Co. Inc.; admits that respondent disallowed said sum of $86,859.75 as a deduction and added the amount to petitioner's taxable net income for the year involved herein. Denies the remaining allegations in paragraph 5(c) of the petition.

(d). Admits that the petitioner claimed as a deduction for depreciation in its income tax return for the taxable year involved the sum of $20,830.42 and further admits that the respondent disallowed a certain portion of the sum thus claimed as a deduction and added the same to petitioner's taxable net income for the year involved herein. Denies the remaining allegations in paragraph 5(d) of the petition.

(e). Admits that petitioner's income and excess profits tax return for the taxable year involved herein disclosed a net loss of $64,403.79 and no tax due or payable. Admits further that respondent [15] has increased petitioner's taxable net income for the year involved herein and has determined a deficiency in tax against the petitioner for the said year. Denies the remaining allegations in paragraph 5(e) of the petition.

Denies generally and specifically each and every allegation set forth in the petition and not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the appeal be denied.

(Signed) HERMAN OLIPHANT
General Counsel for the
Department of the Treasury.

Of Counsel:
JAMES D. HEAD, JR.,
HUGH R. DOWLING,
Special Attorneys,
Bureau of Internal Revenue.

[Endorsed]: U.S.B.T.A. Filed Mar. 24, 1936. [16]

MINUTES OF PROCEEDINGS

United States Board of Tax Appeals

Date, July 5, 1936.
Place, San Francisco, Calif.
Docket No., 82865, 82870, 82871.
Proceeding: Chester N. Weaver Co.—Chester N. Weaver—Elsie S. Weaver.
Assigned to: Hon. C. P. Smith, Division No. 5.
Counsel for Petitioner: A. E. Graupner, Esq., 1110 Balfour Bldg., San Francisco, Calif.
Counsel for Respondent: O. W. Swecker, Esq.
Stenographic Reporter, Payne.
Hearing: CC.
Transcript Ordered: Yes.
On the merits, Yes.

On the motion of counsel to consolidate for hearing.

Ordered: Motion to consolidate granted.

Filed at hearing: Stipulation as to the facts.

Petitioner's brief: August 6, 1936.

Respondent's brief: September 7, 1936. Reply, October 7, 1936.

Witnesses for Petitioner

[Not filled in]

Witnesses for Respondent

[Not filled in]

EXHIBITS

Petitioner's

(Number and Describe)

[Not filled in]

Respondent's

(Letter and Describe)

[Not filled in]

(Signed) CLIFTON N. JACK,

Division Clerk [17]

[Title of Court and Cause.]

FINDINGS OF FACT AND OPINION

Docket Nos. 82865, 82870, 82871. Promulgated February 17, 1937.

The petitioners sustained losses during the taxable year upon liquidation of a corporation in which they owned all of the preferred stock. They had owned the stock for a period of less than two years. No claim is made that they realized gains during the taxable year from the sale of stocks or

bonds which were not capital assets. Held, that the deduction of the loss sustained by each of the petitioners is barred by section 23 (r) (1) of the Revenue Act of 1932.

A. E. Graupner, Esq., for the petitioners.

O. W. Swecker, Esq., for the respondent.

These proceedings, which were consolidated for hearing, involve deficiencies in income tax for the year 1933 as follows:

Petitioner	Docket No.	Deficiency
Chester N. Weaver Co.	82865	$4,323.48
Chester N. Weaver	82870	8,832.43
Elsie S. Weaver	82871	2,447.84

The only question for our determination is whether petitioners, in determining their net income, may deduct the losses sustained by them upon the liquidation of the Jeff R. Townsend Co., in which they held all of the preferred stock. The losses in question were disallowed by the respondent under section 23 (r) of the Revenue Act of 1932.

Other allegations of error are set forth in the petitions, but since no evidence has been offered to sustain them, it will be deemed that they have been waived. The respondent's claim for an increased deficiency in Docket No. 82871 will also be deemed to have been waived by reason of his failure to offer evidence to support it. [18]

FINDINGS OF FACT

The Chester N. Weaver Co., hereinafter referred to as the Weaver Co., is a California corporation. Chester N. Weaver and Elsie S. Weaver are husband and wife and reside in San Francisco, California.

On December 2, 1931, Chester N. Weaver and Elsie S. Weaver purchased 500 shares each of the 6 percent cumulative preferred stock of the Jeff R. Townsend Co., hereinafter referred to as the Townsend Co., paying therefor $100 per share. On August 9, 1932, the Weaver Co. acquired from the same corporation 1,000 shares of its preferred stock at the same price. The 2,000 shares of preferred stock so purchased constituted all of the preferred stock of the Townsend Co. The common stock belonged to other interests. The articles of incorporation provided that in the event of liquidation the holders of preferred stock should be entitled to receive therefor a sum equal to 105 percent of the par value thereof before any amount should be distributed to the holders of the common stock.

Early in 1933 the Townsend Co. became financially involved and unable to continue business. Its stockholders took the necessary steps to effect its dissolution and liquidation. On or about September 17, 1933, it sold all of its assets to the Weaver Co. for $26,280.50. On September 18, 1933, the petitioners in these proceedings, holders of all of the preferred stock of the Townsend Co., sur-

rendered their stock certificates for cancellation and for the purpose of completing liquidation and effecting dissolution of that company. The $26,280.50 received for its assets was distributed in liquidation to the preferred stockholders pro rata. The Weaver Co. received $13,140.25; Chester N. Weaver, $6,570.13, and Elsie S. Weaver, $6,570.12.

In their income tax returns for 1933 each of the petitioners deducted as a loss the difference between the amount paid for the preferred stock so surrendered and the amount received in liquidation, and, in determining the deficiencies herein, the respondent has disallowed the deductions so claimed.

OPINION.

Turner: The only question for determination is whether or not section 23 (r) (1)[1] of the Revenue Act of 1932 bars the deduction of the losses sustained by the petitioners on liquidation of the Townsend Co. There is no claim by the petitioners that the gross income re- [19] ported, and against which the deduction is sought, includes gains from the sale of stocks or bonds which were not capital assets.

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[1]Sec. 23. (r) Limitation on Stock Losses.—(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

It is the contention of the petitioners that the provisions of sections 22(d), 115(c), 111, and 112(a)[2] of the act provide for the deduction in full of losses sustained as the result of a distribution in complete liquidation of a corporation, and that the provisions of section 23, relating to deductions from gross income, are not applicable.

The petitioners' argument that the losses in question are deductible without regard to section 23 starts with section 22 (d), which provides that "distributions by corporations shall be taxable to shareholders as provided in section 115." Referring next to subsection (c) of section 115, they point out that although "amounts distributed in complete liquida-

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[2]Sec. 22. (d) Distributions by Corporations.—Distributions by corporations shall be taxable to the shareholders as provided in section 115.

Sec. 115. (c) Distributions in Liquidation.—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. In the case of amounts distributed in partial liquidation (other than a distribution within the provisions of section 112(h) of stock or securities in connection with a reorganization) the part of such distribution which is properly chargeable to capital accounts shall not be considered a distribution of earnings or profits within the meaning of subsection (b) of this section for the

tion of a corporation shall be treated as in full payment in exchange for the stock" the "gain or loss to a distributee resulting from such exchange" is determined under section 111, and "recognized" to the extent provided in section 112. Our attention is then called to the fact that by the terms of section 112 (a), the entire amount of gain or loss "upon the sale or exchange" of property "shall be recognized" except as thereafter provided in that section. It is then concluded that since the remaining provisions of section 112 contain no limitation or prohibition of the recognition of a loss resulting from complete liquidation of a corporation, the entire amount of the loss is recognized, and being recognized in full, its deduction is in no way de-

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purpose of determining the taxability of subsequent distributions by the corporation.

Sec. 111. (a) Computation of Gain or Loss.—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113(b), and the loss shall be the excess of such basis over the amount realized.

* * * * * * *

(c) Recognition of Gain or Loss.—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

Sec. 112. (a) General Rule.—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

pendent upon or limited by the provisions of section 23. [20]

The fallacies in this argument are elementary and obvious, and are at once apparent upon examination of the structure and plan of the income tax statute. The tax is imposed on net income and, according to section 21, net income is "gross income computed under section 22, less the deductions allowed by section 23." Section 22 provides generally that gross income "includes gains, profits, and income * * * of whatever kind and in whatever form paid, or from * * * any source whatever." It also enumerates certain specific items that are to be included in gross income and others that are to be excluded. Section 23 enumerates and describes the allowable deductions referred to in section 21. It is argued in this connection that sections 112 to 120, inclusive, are relief or distinctive provisions, and to rule that their application is to be made with reference to section 23 would amount to their repeal or nullification. We find nothing in any of these sections to indicate that the so-called or distinctive provisions are to be applied without reference to section 22 if they involve items of gain or profit, or without reference to section 23 if they involve losses or other charges allowable against gross income. On the other hand, Congress has particularly and specifically brought the application of these so-called relief sections within the provisions of sections 22 and 23. Illustrations are numerous. Subsection (b) (7) of section 22 provides for the exclusion from

gross income of the items of gain set forth in section 116, while subsections (g), (h), (i), (l), (m), and (n) of section 23 specifically give effect to the provisions of sections 113, 118, 117, 114 (b), (3), and (4), 114, and 120, respectively. It is thus apparent from the general plan of the statute that, in the absence of specific language to the contrary, deductions from gross income are allowable by and through the provisions of section 23 only. No other method of determining net income is provided.

The petitioners seek to vary the general plan of the statute by arguing that losses resulting to stockholders from corporate liquidations are to be given effect through section 22 (d). That argument is, in short, a claim that a loss deduction may be taken in the form of a minus or negative item of gross income, under the gross income provisions of the statute and without regard to the provisions of section 23. Obviously the provision in section 22 (d), to the effect that "distributions by corporations shall be taxable to shareholders as provided in section 115", is not susceptible of such strained construction.

The argument made here would also permit the deduction of a loss from the sale of stocks or securities on the market, without regard to section 23, since section 112 (a) provides that such a loss is to be recognized in full, there being no subsequent provision in that section [21] providing otherwise. Such reasoning would completely nullify the provisions of section 23 (e), (f), and (r) (1). The recognition

or nonrecognition of gain or loss under section 112 is in no sense a determination that the gain is to be included in gross income or that the loss is to be deducted therefrom. It is merely a determination as to whether or not the gain or loss is to be given such tax significance as the statute provides in the year in which the transaction giving rise to the gain or loss occurred, or is to be postponed until the happening of a further transaction in a subsequent year. Even though recognized, the tax effect of the gain or loss in computing net income is to be determined through the application of the gross income and deduction provisions of the statute. The result here being a recognized loss, the extent to which that loss is deductible is determined by the provisions of section 23.

In their reply brief the petitioners make the further contention that the limitation prescribed by section 23 (r) (1), on loss deductions, is not applicable here on the ground that a loss sustained in the disposition of stock in a corporate liquidation is not a loss from the sale or exchange of stock within the meaning of the statute. The reasoning advanced is that Congress, through sections 22 (d) and 115 (c), on the one hand, and sections 22 (e) and 111 (a) and (b) on the other, has carefully drawn a distinction between the disposition of stock in liquidation and an ordinary sale or exchange of stock on the market, and that the disallowance or limitation under section 23 (r) (1), of a loss sustained in the disposition of stock in liquidation requires the dis-

tortion or disregard of other pertinent provisions of the statute. It is also claimed that section 23 (r) (1) is applicable only to losses sustained in a sale or exchange of stocks and bonds on the market, because the Congressional Committees, in stating reasons for the insertion of section 23 (r) (1) in the statute, made specific reference to sales or exchanges on the market and no reference to the disposition of stock in a corporate liquidation.

It is well established that the reports of Congressional Committees may be resorted to as an aid to construction when the terms of the statute are contradictory or ambiguous, or the meaning of the words used is doubtful. Caminetti v. United States, 242 U. S. 470; Penn Mutual Life Insurance Co. v. Lederer, 252 U. S. 523. But it is equally well established that the intent of the lawmaker must be sought in the language of the statute, and where that language is clear and unambiguous, it must be enforced according to its terms and may not be varied or limited by reference to committee reports. The plain language of the statute may not be cast aside for other language thought by some one to have been in the mind of the legislative body. Congress must be presumed to have meant what it has said. Crooks v. [22] Harrelson, 282 U. S. 55; United States v. Goldenberg, 168 U. S. 95; Helvering v. City Bank Farmers Trust Co., 296 U. S. 85; Edith M. O'Donnell, 35 B. T. A. No. 37. From a consideration of the cases before us and the provisions of the statute involved, it does not appear here that

the aid of the Committee reports is invoked because the language of section 23 (r) (1) is ambiguous, but because the petitioners desire to limit and restrict the application of that language to the situations covered by specific illustrations in those reports. Clearly the cases cited do not permit reference to legislative history for such purposes, and where there is no ambiguity the language of the statute is controlling.

In support of their claim for a narrow and restricted application of section 23 (r) (1), the petitioners have cited numerous court decisions which deal with the interpretation and construction of statutes. It is our opinion that the cases cited generally support the respondent rather than the petitioners. In Helvering v. Stockholm Enskilda Bank, 293 U. S. 84, the Supreme Court stated that the intention of Congress, with reference to a particular provision of a taxing statute, is to be determined not by viewing the provision apart and separate from its setting in the act, but by considering it in connection with the context, general purpose of the statute in which it is found, and the occasion and circumstances of its use. In section 115 (c), on which petitioners base their claim for distinction, it is provided that amounts distributed in complete liquidation of a corporation are to be treated "as in full payment in exchange for the stock." It is then provided that the amount of gain or loss is to be "determined under section 111" and recognized "to the extent provided in section 112." These sec-

tions deal generally with the "sale or exchange" or "the sale or other disposition" of property. It thus appears by direct reference to other sections of the statute, that the disposition of corporate stock in liquidation is to be treated, for income tax purposes, as a "sale or exchange" and the distinction claimed by the petitioners is refuted by the plain words of the statute. Furthermore, it is interesting to note that if any doubt did exist and there were any basis for a claim of ambiguity, the report of the Committee on Ways and Means of the House of Representatives submitted with the bill which became the Revenue Act of 1924, in which report the language used in section 115 (c) was inserted, definitely indicates that the disposition of stock in a corporate liquidation is, for income tax purposes, a sale. The Committee there said: "The proposed bill, as did the 1918 Act, treats a liquidating dividend as a sale of the stock to the corporation and recognizes the true effect of such a distribution." [23]

The deduction of recognized losses in the case of an individual is governed by the provisions of subsection (e) of section 23, and, if a corporation, by the provisions of subsection (f). In both of these subsections it is provided that the deductions so allowed are subject to the limitation provided in subsection (r), paragraph (1) of which has been quoted above. The language of that limitation is plain and the deduction of any loss resulting from the sale or exchange of stocks or bonds, not capital assets, is limited in amount to gains derived from the sale or exchange of similar assets. In the cases

before us the preferred stock of the Townsend Co. was disposed of in liquidation of that company. The stock did not constitute capital assets in the hands of the petitioners and they make no claim that they realized any gains from the sale of similar assets. This disposition of the stock, under the provisions of the statute considered above, was a sale or exchange and the deduction of the losses sustained is barred by the provisions of section 23 (r) (1) of the statute.

Reviewed by the Board.

Decision will be entered under Rule 50.

Smith, dissenting: It is a cardinal principle of statutory construction that taxing statutes should be interpreted according to the intent of the legislative body enacting them. Thus, in Smythe v. Fiske, 23 Wall. 374, the Supreme Court said:

> A thing may be within the letter of a statute and not within its meaning, and within its meaning, though not within its letter. People v. The Utica Insurance Co., 15 Johnson, 380; Atkins v. The Fibre Disintegrating Co., 18 Wallace, 301; Bacon's Abridgment, title Statutes, 1, 2, 3, 5. The intention of the lawmaker is the law.

In Helvering v. New York Trust Co., 292 U. S. 455, the Supreme Court said:

> The rule that, where the statute contains no ambiguity, it must be taken literally and given

effect according to its language, is a sound one not to be put aside to avoid hardships that may sometimes result from giving effect to the legislative purpose. Commr. of Immigration v. Gottlieb, 265 U. S. 310, 313, 44 S. Ct. 528, 68 L. Ed. 1031; Bate Refrigerating Co. v. Sulzberger, 157 U. S. 1, 37, 15 S. Ct. 508, 39 L. Ed. 601. But the expounding of a statutory provision strictly according to the letter without regard to other parts of the act and legislative history would often defeat the object intended to be accomplished. Speaking through Chief Justice Taney in Brown v. Duchesne, 19 How. 183, page 194, 15 L. Ed. 595, this court said: "It is well settled that, in interpreting a statute, the court will not look merely to a particular clause in which general words may be used, but will take in connection with it the whole statute (or statutes on the same subject) and the objects and policy of the law, as indicated by its various provisions, and give to it such a construction as will carry [24] into execution the will of the Legislature, as thus ascertained, according to its true intent and meaning." Quite recently in Ozawa v. United States, 260 U. S. 178, page 194, we said: "It is the duty of this Court to give effect to the intent of Congress. Primarily this intent is ascertained by giving the words their natural significance, but if this leads to an unreasonable result plainly at variance with the policy of the legislation as

a whole, we must examine the matter further. We may then look to the reason of the enactment and inquire into its antecedent history and give it effect in accordance with its design and purpose, sacrificing, if necessary, the literal meaning in order that the purpose may not fail."

And in Barrett v. Van Pelt, 268 U. S. 85, 90, 45 S. Ct. 437, 439, 69 L. Ed. 857, we applied the rule laid down in People v. Utica Ins. Co., 15 Johns. (N. Y.) 358, 381, 8 Am. Dec. 243, that "a thing which is within the intention of the makers of a statute is as much within the statute as if it were within the letter, and a thing which is within the letter of a statute, is not within the statute, unless it is within the intention of the makers."

Did the Congress by section 23 (r) intend to prevent corporate stockholders sustaining losses upon the liquidation of corporations from deducting those losses from gross income except to the extent of gains realized from sales or exchanges of stocks and bonds? I think not.

The legislative history of section 23 (r) of the Revenue Act of 1932 shows that that provision was designed to prevent corporate stockholders from deducting from gross income losses created through sales or exchanges "in the stock and bond markets." The Ways and Means Committee Report 708 on H. R. 10236, which later became the Revenue Act of 1932, comments upon five proposed additions to

section 23 of the Revenue Act of 1928, i.e., subsections (r), (s), (t), (u), and (v). These proposed subsections emerged in amended form as subsections (r), (s), and (t) of the Revenue Act of 1932. In presenting the five proposed additions to the House Bill, the Ways and Means Committee Report stated, p. 12:

> Many taxpayers have been completely eliminating from tax their income from salaries, dividends, rents, etc., by deducting therefrom losses sustained in the stock and bond markets, with serious effect upon the revenue. Your committee is of the opinion that some limitation ought to be placed on the allowance of such losses.

After referring to the exclusion of "dealers in securities", as provided in subsection 23 (r) (3), the Committee reports stated:

> Traders or other taxpayers who buy and sell securities for investment or speculation, whether or not in their own account, and irrespective of whether such buying or selling constitutes the carrying on of a trade or business, are not regarded as dealers in securities within the meaning of this rule.

The Finance Committee Report of the Senate on this same bill (Report 665, p. 12) contains the following: [25]

> The House Bill adopted very severe limitations upon the allowance of losses from the sale

> of securities, as a deduction in computing net income. The provision is based upon a twofold policy: (1) Protecting the revenues from the growing practice of reducing tax liabilities by the sale of securities on which losses had accrued, and (2) preventing speculative losses from wiping out ordinary income, which represents real tax-paying ability.

There is nothing in the Committee reports which tends in the slightest to show that section 23 (r) had in contemplation losses sustained through the liquidation of corporations.

Section 22 (d) of the Revenue Act of 1928 provides that "Distributions by corporations shall be taxable to the shareholders as provided in section 115", and section 115 (c) provides in part:

> Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. * * *

The Revenue Act of 1928 contained no provision corresponding to section 23 (r) of the Revenue Act of 1932. Section 22 (d) and section 115 (c) of the Revenue Act of 1928 were incorporated and made a part, without change, of the Revenue Act of 1932.

Where corporations are liquidated, stockholders receiving liquidation distributions may or may not turn in their shares of stock. It is a common thing

for them to do so. See Phelps v. Commissioner, 54 Fed. (2d) 289. Whether they do so or not, however, they are treated as exchanges under both the Revenue Act of 1928 and that of 1932 for the purpose of giving corporate stockholders the benefits of sections 111 and 112.

The word "exchange" in its ordinary meaning carries with it the idea of mutual agreement--a transfer of property for property in a transaction freely arrived at between two parties. See Law v. McLaughlin, 2 F. Supp. 601. These elements are lacking where in distributions in liquidation a stockholder has no alternative but to surrender his shares of stock and receive his proportion of the assets of the corporation distributable to him. Section 115 (c) does not provide that distributions in liquidation shall constitute "exchanges." It simply provides that they shall be treated as in full or part payment "in exchange" for the stock.

In section 23 (r) of the Revenue Act of 1932 the word "exchange" is coupled with the word "sales." Under the doctrine of ejusdem generis the word "exchanges" must be interpreted in the light of the word with which it is associated. Losses sustained upon sales of stocks and bonds are subject to the limitation of section 23 (r) (1). If the word "exchanges" had not been used in this provision the very evil at which section 23 (r) was aimed might have been perpetuated [26] by corporate stockholders exchanging their stocks and bonds for other securities or other property. Such circumvention of

the statute was forestalled by the language used by the draftsmen of the act.

In the light of the legislative history of section 23 (r) I can not believe that Congress had any intention of limiting the deduction from gross income of losses sustained by taxpayers in the liquidation of corporations.

Black, Tyson, Hill, and Harron agree with this dissent. [27]

United States Board of Tax Appeals
Docket No. 82865, 82870, 82871.

CHESTER N. WEAVER COMPANY,
CHESTER N. WEAVER,
ELSIE S. WEAVER,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the Findings of Fact and Opinion of the Board promulgated February 17, 1937, the respondent herein, on February 27, 1937 filed a notice of settlement and proposed recomputation, and the petitioner herein, having on March 12, 1937 filed an acquiescence in the recomputation as made by the respondent, it is

ORDERED and DECIDED, that there are deficiencies in income tax for the year 1933 as follows:

Name	Docket No.	Amount:
Chester N. Weaver Company,	82865	$4,323.48
Chester N. Weaver,	82870	8,832.43
Elsie S. Weaver,	82871	2,447.84

Enter:

[Seal] BOLON B. TURNER,
Member.

Entered Mar 20 1937. [28]

[Title of Court and Cause.]

PETITION OF CHESTER N. WEAVER COMPANY, A CORPORATION, FOR REVIEW BY THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT OF A DECISION BY THE UNITED STATES BOARD OF TAX APPEALS IN THE ABOVE ENTITLED PROCEEDING.

Chester N. Weaver Company, a corporation, the petitioner in the above entitled proceeding hereby files this petition for a review by the United States Circuit Court of Appeals for the Ninth Circuit of a decision of the United States Board of Tax Appeals rendered against it (promulgated February 17, 1937, 35 B. T. A. No. 76 and entered March 20, 1937,) determining a deficiency in petitioner's Federal income tax for the calendar year

1933 in the amount of $4,323.48, and in and by this petition respectfully shows:

I.

JURISDICTION

Petitioner Chester N. Weaver Company is and at all the times herein mentioned was a corporation duly organized [29] and existing under the laws of the State of California, with its principal place of business in the City and County of San Francisco in said State. Petitioner filed its Federal income tax return for the calendar taxable year 1933 with the United States Collector of Internal Revenue for the First District of California in the office of said Collector located in said City and County of San Francisco and within the jurisdiction of the United States Circuit Court of Appeals for the Ninth Circuit.

II.

PRIOR PROCEEDINGS

Respondent, on December 30, 1935, claimed and determined additional income tax for the taxable calendar year 1933 against petitioner in the amount of $4,323.48, and as required by section 272 of the Revenue Act of 1932 respondent on said day sent to petitioner by registered mail a notice of such deficiency. On February 4, 1936, petitioner appealed to the United States Board of Tax Appeals from such proposed determination of deficiency and on March 24, 1936, respondent filed his answer to such appeal.

Thereafter, and on July 6, 1936, the appeal of petitioner was consolidated for hearing and decision with the appeals of Chester N. Weaver, Docket No. 82870, and Elsie S. Weaver, Docket No. 82871, by order of the United States Board of Tax Appeals and the three appeals were then submitted for decision on a stipulation of facts applicable to the one and only question at issue in said three appeals.

Thereafter and on February 17, 1937, said Board of Tax Appeals promulgated its finding of fact and opinion in the consolidated proceedings and on March 20, 1937, entered its [30] final order and decision therein and ordered and decided that there was a deficiency in petitioner's Federal income tax for the year 1933 in the amount of $4,323.48.

III.

NATURE OF CONTROVERSY

The controversy involves the proper determination of petitioner's Federal income tax for the calendar year 1933. The question is whether petitioner sustained a deductible loss in the amount of $86,859.75 in a transaction entered into for profit.

During the year 1931 and years prior thereto Chester N. Weaver Company (hereinafter referred to as Weaver Company) was engaged in the business of distributing and selling Studebaker and Pierce-Arrow automobiles in the City and County of San Francisco and the cities of Oakland and Berkeley, Alameda County, State of California.

In November of 1931 Weaver Company decided to dispose of its business of distributing and selling automobiles. One Jeff R. Townsend organized a corporation under the name of "Jeff R. Townsend Company, Inc." (hereinafter referred to as Townsend Company) on November 25, 1931, for the purpose of purchasing the automobile business of Weaver Company. The new corporation had an authorized capital stock of 5,000 shares of a par value of $100. per share, of which 3,000 shares were common and 2,000 shares were preferred. Jeff R. Townsend and Earl R. Carpenter subscribed and paid for 500 shares of said common stock at par. On August 9, 1932, petitioner purchased from said Townsend Company 1000 shares of its preferred stock [31] and paid $100,000 therefor. From said last mentioned date to September 18, 1933, when said Townsend Company was liquidated, a period of less than two years, petitioner was at all times the owner and holder of said 1,000 shares of said preferred stock.

During the early part of 1933, prior to March 28, 1933, the Townsend Company became financially involved and unable to continue its business. On March 28, 1933, at a meeting of its stockholders, it was determined to close the affairs of the Townsend Company and voluntarily liquidate and dissolve the corporation. Thereafter and during the month of September, 1933, said corporation was finally liquidated and dissolved by voluntary proceedings.

In the liquidation of said Townsend Company and after payment of its liabilities but $26,280.50 of its capital remained for distribution to its stockholders. As this amount was inadequate to satisfy the preference of the preferred stockholders, said $26,280.50 was distributed pro rata to the preferred stockholders in complete liquidation of said corporation and none of the assets of such corporation were distributed to the common stockholders. On said distribution in final liquidation of said Townsend Company petitioner received only the amount of $13,140.25.

Petitioner kept its accounts and made its income tax return for the calendar year 1933 on a cash receipts and disbursements basis and deducted the difference between the amount of $100,000 paid for said 1000 shares of said preferred stock and said amount of $13,140.25 received for said shares in liquidation, or $86,859.75, as a loss sustained in the taxable year 1933. Respondent disallowed said deduction. [32]

Petitioner contended before the United States Board of Tax Appeals that it was entitled to deduct the loss of $86,859.75 asserted and deducted by it in its income tax return for 1933 under the provisions of sections 22(d), 115(c), 111 and 112(a) of the Revenue Act of 1932.

Said Board of Tax Appeals held that section 23(r) (1) of said revenue act barred the deduction sought.

Petitioner, being aggrieved by the findings of fact and conclusions of law contained in the findings and

opinion of said Board of Tax Appeals and by its decision entered pursuant thereto, desires to obtain a review thereof by the United States Circuit Court of Appeals for the Ninth Circuit.

IV.

ASSIGNMENTS OF ERROR

Petitioner assigns as error the following acts and omissions of the United States Board of Tax Appeals:

(1) The failure to allow the amount of $86,859.75 as a deductible loss sustained by petitioner during the taxable year 1933 and as a deduction from petitioner's gross income for said year within the intendment of section 23 of the Revenue Act of 1932.

(2) The failure to give proper effect to the provisions of sections 22(d), 115(c), 111 and 112(a) of the Revenue Act of 1932 in determining petitioners net taxable income for the calendar year 1933.

(3) The failure to interpret section 23(r) (1) of the Revenue Act of 1932 in accordance with the purpose and intent of that section and the meaning of Congress in enacting that section. [33]

(4) The failure to find that petitioner sustained a deductible loss in the amount claimed for the year 1933.

(5) The holding that petitioner is liable for a deficiency for the year 1933 in lieu of a determination that there is no income tax due from petitioner for the year in controversy.

Wherefore, petitioner prays that the decision of the United States Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Ninth Circuit; that a transcript of the record be prepared in accordance with law, the rules of said Court and the rules and practice of said Board of Tax Appeals for filing, and that appropriate action be taken to the end that the errors complained of herein be reviewed and corrected by said Court.

ADOLPHUS E. GRAUPNER
ARTHUR E. COOLEY
Counsel for Petitioner,
1110 Balfour Building,
San Francisco, California

[34]

State of California
City and County of San Francisco—ss.

Chester N. Weaver, being first duly sworn deposes and says that he is the President of the Chester N. Weaver Company, a corporation and the petitioner herein, and as such is authorized to verify the foregoing petition; that he has read the foregoing petition and knows the contents thereof; that to the best of his knowledge and belief the statements therein are true and the assignments of error are well taken and intended to be argued.

CHESTER N. WEAVER

Subscribed and sworn to before me this 12th day of April, 1937.

[Seal] EMILY K. McCORRY

Notary Public in and for the City and County of San Francisco, State of California.

My Commission expires January 16, 1939.

[Endorsed]: U.S.B.T.A. Filed Apr. 20, 1937. [35]

[Title of Court and Cause—Docket Nos. 82865, 82870, 82871.]

STIPULATION OF FACTS.

It is hereby stipulated and agreed by and between parties hereto, by their respective attorneys of record, that the following facts shall be taken as true; provided, however, that this stipulation shall be without [36] prejudice to the right of either party to introduce other and further evidence not inconsistent with the facts herein stipulated to be true; and provided, further, that when offered in evidence this stipulation shall be subject to objection by either party hereto as to relevancy or materiality of all or any part hereof.

It is further stipulated and agreed that, subject to the conditions of the preceding paragraph, and insofar as the facts stated are relevant and material respectively to the above entitled proceedings, the following facts shall be considered as evidence in the said proceedings, Docket Nos. 82865, 82870, 82871:

1. Chester N. Weaver Company (hereinafter referred to as Weaver Company), petitioner in proceeding numbered 82865, is and at all the times hereinafter mentioned was a corporation duly organized and existing under the laws of the State of California.

2. Chester N. Weaver, petitioner in proceeding numbered 82870, is and at all the times hereinafter mentioned was an individual domiciled in the City and County of San Francisco, State of California.

3. Elsie S. Weaver, petitioner in proceeding numbered 82871, is and at all the times hereinafter mentioned was an individual domiciled in the City and County of San Francisco, State of California.

4. Said Chester N. Weaver and Elsie S. Weaver [37] are and at all the times hereinafter mentioned were husband and wife, living together as such and residing in the said City and County of San Francisco.

5. Jeff R. Townsend Company, Inc. (hereinafter referred to as Townsend Company) was incorporated under the laws of the State of California on November 25, 1931, with an authorized capital stock of five thousand shares of a par value of $100. per share, of which authorized shares, three thousand were shares of common stock and two thousand were shares of preferred stock. During the month of September, 1933, the said Townsend Company was liquidated, its assets were distributed and it was formally dissolved as a corporation by voluntary proceedings.

6. The articles of incorporation of the said Townsend Company provided for the two classes of shares of its capital stock, as follows:

Fifth: That the following is a statement of the preferences, privileges and restrictions granted to or imposed upon the holders of the respective classes of shares:

(a) All rights to vote and all voting power are hereby vested exclusively in the holders of the common stock, provided, however, that if there shall be a default or omission in the payment of four quarterly dividend payments on said preferred stock, then the preferred stockholders shall be given notice of all stockholders meetings to be held thereafter and shall have the same rights as the common stockholders to vote at said meetings, but such right to vote shall continue only during such period as the corporation [38] shall be in default in the payment of said dividends. This right to vote shall not deprive the preferred stockholders of the exercise of any right which they may have at law or in equity to enforce any of the provisions with respect to preferred stock.

(b) When fully paid, the preferred stock of this corporation shall be nonassessable.

(c) The holders of the preferred stock of this corporation shall be entitled to receive dividends thereon from the surplus profits of the corporation arising from its business, to the extent that the corporation may lawfully pay

the same, at the rate of six per cent of the par value thereof, per annum, and no more, from the date when issued, payable in equal quarterly installments on the first days of January, April, July and October of each calendar year, provided, however, that the first dividend thereon shall be paid on April 1st, 1932, which first dividend shall be at said rate of six per cent per annum from the date of issuance of the preferred stock then outstanding. Such dividends shall be cumulative and shall be paid in full, for each such dividend period, and for all cumulations of unpaid dividends, before any dividends upon the common stock shall be paid or set apart for payment.

(d) Whenever all dividends accrued upon the preferred shares shall have been paid, or payment thereof tendered, the board of directors of this corporation may declare and pay to the holders of the outstanding common shares dividends thereon from the remaining undistributed profits of the corporation, but said dividends upon common shares shall not be cumulative.

(e) In the event of the dissolution of this corporation or the winding up of its affairs or of the distribution of its assets for any other reason, the holders of such preferred stock shall be entitled to receive, for each share thereof, out of the assets of the corporation, and before any of said assets shall be distributed to the holders of common stock, a sum equal to one hundred five per cent. of the par

value thereof, plus an amount equal to all unpaid dividends then accrued thereon, provided that if said distribution shall be made more than five years after the date of incorporation of this corporation, then the holders of such preferred stock shall be entitled to receive a sum equal to the par value thereof, plus said unpaid dividends then accrued; and, after said payments to said holders of preferred stock shall have been made [39] all of the residue of such assets shall be paid and distributed ratably to and among the holders of the common stock.

(f) The corporation may, at its option, redeem any number of such preferred shares upon any dividend paying date by paying to the holder thereof, for each share redeemed, a sum equal to one hundred five per cent. of the par value thereof, plus an amount equal to all unpaid dividends then accrued thereon, provided that if said redemption shall be made more than five years after the date of incorporation of this corporation, then such shareholder shall be paid a sum equal to the par value of such shares, plus said unpaid dividends then accrued. As a condition precedent to the right of the corporation to redeem said preferred stock, it shall give the shareholder, whose shares it proposes to redeem, written notice of its intention so to redeem at least thirty days prior to

the dividend date upon which redemption is to be made. Said preferred shares so redeemed shall not be reissued.

7. During the year 1931 said Weaver Company was engaged in the business of selling automobiles in the City and County of San Francisco and in the Cities of Oakland and Berkeley, Alameda County, as distributor and agent of Studebaker and Pierce-Arrow automobiles. During the month of November, 1931, the Weaver Company determined to dispose of its agency and business. The above-described Townsend Company was organized by Jeff R. Townsend, San Diego distributor of and agent for Studebaker automobiles, for the purpose of purchasing the San Francisco agency and business of the Weaver Company. On or about December 17, 1931, said Townsend Company purchased all of the physical assets of the Weaver Company, excepting real property, which were located in San Francisco, including its entire stock of automobiles, furniture [40] and fixtures, machinery and tools, and equipment located in the Weaver Building, Bush Street and Van Ness Avenue, San Francisco. On or about July 26, 1932, said Townsend Company purchased all of the physical assets of the Weaver Company excepting real property, which were located in Alameda County, in the cities of Oakland and Berkeley including its entire stock of automobiles, furniture and fixtures, machinery and tools, and equipment.

8. At the time of organization of said Townsend Company, Jeff R. Townsend and Earl R. Carpenter subscribed and paid for five hundred shares of the common stock of said company at par and each of said Chester N. Weaver and said Elsie S. Weaver subscribed for five hundred shares of the preferred stock of said company. On December 2, 1931, Chester N. Weaver paid $50,000. and Elsie S. Weaver paid $50,000. to said Townsend Company for said shares of stock and certificates for five hundred shares of preferred stock were thereupon delivered to each of said Chester N. Weaver and Elsie S. Weaver.

9. Thereafter and until the certificates for said shares of preferred stock were surrendered for cancellation on liquidation of the said Townsend Company on September 18, 1933, each of said Chester N. Weaver and said Elsie S. Weaver continued to be the owner and holder of five hundred shares of preferred stock of said Townsend Company.

10. On August 9, 1932, said Weaver Company purchased from said Townsend Company one thousand shares of [41] its preferred stock and paid to said Townsend Company for said shares the sum of $100,000. Thereafter and until the certificate for said shares of preferred stock were surrendered for cancellation on liquidation of the said Townsend Company on September 18, 1933, said Weaver Company continued to be the owner and holder of one thousand shares of the preferred stock of said Townsend Company.

11. Dividends at the rate of six per centum per annum were declared by the Townsend Company upon its issued preferred capital stock on April 2, 1932, July 2, 1932, and October 3, 1932.

12. During the early part of 1933 and prior to March 28, 1933, said Townsend Company became financially involved and unable to continue its business and on March 28, 1933, a meeting of the stockholders was held for the purpose of considering the question of closing up the affairs of the company and voluntarily dissolving the corporation. At such meeting a resolution was adopted by vote of the holders and owners of all the common stock of the corporation authorizing the liquidation and dissolution of the company and directing the President and Secretary to execute the corporate certificate giving notice of intention to dissolve as required by law. At said meeting, by resolution adopted by vote of the holders and owners of all the common stock of the corporation, Chester N. Weaver was appointed agent of said Townsend Company for the purpose of supervising [42] the closing of its business affairs to effect its dissolution.

13. On March 28, 1933, following the above-mentioned stockholder's meeting, a meeting of the directors of the said Townsend Company was held. At such meeting the directors of the corporation appointed Chester N. Weaver as agent to close the business affairs of the company and take all necessary steps to effect its dissolution.

14. Thereafter proceedings were taken for the liquidation of the business affairs of the Town-

send Company and on September 16, 1933, the directors, at a special meeting called for that purpose, adopted a resolution authorizing the corporation to sell "all of its remaining assets, tangible and intangible to the Chester N. Weaver Co. for the sum of $26,280.50 and the assumption by Chester N. Weaver Co. of all the outstanding debts and liabilities of Jeff R. Townsend Company, Inc." Thereafter and about September 17, 1933, said Townsend Company transferred and delivered all of its remaining assets to said Weaver Company and said Weaver Company paid the amount of $26,280.50 therefor to said Townsend Company.

15. On September 18, 1933, all of the stockholders of the Townsend Company surrendered their certificates for shares of stock in the corporation for cancellation for the purpose of completing liquidation and effecting dissolution of said company. The said Weaver Company surrendered for cancellation two preferred stock certificates, each for [43] five hundred shares; said Chester N. Weaver surrendered for cancellation one preferred stock certificate for five hundred shares, and said Elsie S. Weaver surrendered for cancellation one preferred stock certificate for five hundred shares. Jeff R. Townsend surrendered for cancellation one common stock certificate for two hundred shares and Earl R. Carpenter surrendered for cancellation one common stock certificate for three hundred shares. The certificates thus surrendered represented all of the capital stock of said Townsend Company.

16. On surrender of the preferred stock certificates as above described, the entire assets of said Townsend Company, consisting of $26,280.50, were distributed to the owners and holders of such preferred stock, as follows: to said Weaver Company, $13,140.25; to Chester N. Weaver, $6,570.13; and to Elsie S. Weaver, $6,570.12. The assets of the said corporation being insufficient to pay the holders of the preferred stock "a sum equal to one hundred and five per cent of the par value thereof", or the par value thereof, no part of the said assets was distributed to the common stockholders.

17. Each of the four certificates for preferred stock surrendered as above described was endorsed on the back thereof as follows:

"San Francisco, California,
September 18, 1933

"This certificate surrendered to Jeff Townsend Co. Inc. upon payment of $ as final [44] payment on this stock as per distribution of assets."

The amount of $6,570.12 was written after the symbol $ in the endorsement on Chester N. Weaver's certificate, $6,570.13 in Elsie S. Weaver's certificate and $6,570.12 on one certificate of Chester N. Weaver Co. and $6,570.13 on the other certificate of Chester N. Weaver Co. Each of said endorsements was signed by the owner and holder of the certificate surrendered. The two certificates for common stock of said Townsend Company, surrendered respectively by Jeff R. Townsend and Earl R. Carpenter, bore no endorsement other than the

usual blank form of endorsement for transfer signed by the respective stockholders:

18. None of the petitioners in the above named proceedings received any other assets or amount than that as set forth hereinabove in paragraph numbered 16 from the liquidation, distribution of assets and dissolution of said Townsend Company.

19. In its income tax return for the taxable year 1933, said Weaver Company deducted from its returned income the amount of $86,859.75 as a loss resulting from the liquidation of said Townsend Company.

In his income tax return for the taxable year 1933, said Chester N. Weaver deducted from his returned income the amount of $43,429.87 as a loss resulting from the liquidation of said Townsend Company.

In her income tax return for the taxable year [45] 1933, said Elsie S. Weaver deducted from her returned income the amount of $43,429.87 as a loss resulting from the liquidation of said Townsend Company.

Respondent disallowed the deductions taken by the respective petitioners as above set forth and thereupon determined the deficiencies at issue in the above entitled proceedings.

20. The respondent disallowed the losses deducted by the respective petitioners in the above entitled proceedings as set forth in the preceding paragraph and the sole issue for determination by the United States Board of Tax Appeals in each

of the above entitled proceedings is whether said deductions are properly allowable under the Revenue Act of 1932.

21. The copies of the deficiency notice attached to each of the petitions in the above entitled proceedings are stipulated to be true copies of such notices and are admitted as evidence on behalf of the respective petitioners as Exhibit No. 1 in each of the above entitled proceedings.

22. Photostatic copies of the income tax [46] returns of the respective petitioners filed herewith by respondent are stipulated to be true copies and are respectively admitted as evidence on behalf of respondent as Exhibit A in each of the above entitled proceedings.

ADOLPHUS E. GRAUPNER
ARTHUR E. COOLEY
Attorneys for Petitioners
Chester N. Weaver Company
Chester N. Weaver
Elsie S. Weaver.

HERMAN OLIPHANT O. W. S.
General Counsel for the Department of the Treasury
Attorney for Respondents.

[Endorsed]: U. S. B. T. A. Filed at hearing July 6, 1936. [47]

[Title of Court and Cause Docket Nos. 82865, 82,-870, 82871.]

STIPULATION AND ORDER FOR CONSOLIDATION ON REVIEW

Whereas, the above entitled three proceedings involve similar facts and presented the same question and issue for decision by the United States Board of Tax Appeals; and [48]

Whereas, under order of said Board the above entitled proceedings were consolidated for hearing and decision and but one findings of fact, opinion and decision was made by said Board in and for said three proceedings; and

Whereas, separate petitions for review of said consolidated findings, opinion and decision by the United States Circuit Court of Appeals for the Ninth Circuit, with separate assignments of errors have been filed with said Board on behalf of each of the above named petitioners in the proceedings respectively instituted by them; and

Whereas, each of said petitions sets forth the same material facts and assignments of errors as the others, and the three petitions differ only in the titles of the petitioners and the amounts claimed as deductible losses therein; and

Whereas, the preparation and printing of the complete record in proceeding No. 82865, Chester N. Weaver Company v. Commissioner of Internal Revenue will be sufficient for the said Court to consider and dispose of the questions involved in the

three above entitled proceedings and will avoid the unnecessary expense of preparing and printing three separate records for review of the same questions of law;

Now, Threfore, It Is Hereby Stipulated and Agreed by and between all of the parties above named by their respective counsel as follows:

1. The Clerk of said United States Board of Tax Appeals shall prepare and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, a complete record in proceedings No. 82865, Chester N. Weaver Company v. [49] Commissioner of Internal Revenue as follows:

(a) The docket entries of proceedings had before said Board in said proceedings No. 82865;

(b) The pleadings before said Board in said proceedings No. 82865 as follows:
(1) Petition for redetermination,
(2) Answer of the respondent;

(c) Minute order of said Board consolidating the three above entitled proceedings for hearing and decision;

(d) The findings of fact and opinion of said Board in proceedings No. 82865.

(e) The decision of said Board;

(f) The petition for review and assignment of errors filed by the petitioner Chester N. Weaver Company in proceedings No. 82865;

(g) The consolidated stipulation of facts filed with said Board in the above entitled pro-

ceedings, Docket Nos. 82865, 82870 and 82871;

(h) This stipulation and order;

(i) The praecipe for transcript of the record.

2. The Clerk of said United States Board of Tax Appeals shall prepare and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit a skeleton record in each of the proceedings of Chester N. Weaver v. Commissioner of Internal Revenue, Docket No. 82870, and Elsie S. Weaver v. Commissioner of Internal Revenue, Docket No. 82871, as follows:

(a) Petition for review and assignment of errors filed by the respective petitioners in each of said two proceedings;

(b) Proof of service of said petitions for review and assignments [50] of errors in each proceeding;

(c) This stipulation and order; and

(d) The praecipe for transcript of the skeleton record in each proceeding;

3. That the Clerk of said United States Circuit Court of Appeals shall cause to be printed only the record in proceedings No. 82865, Chester N. Weaver Company v. Commissioner of Internal Revenue.

4. That no briefs need be filed by either party with the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit in the proceeding docketed as Nos. 82870 and 82871 in the said Board of Tax Appeals.

5. That the record on appeal from the decision of said Board of Tax Appeals in proceedings No. 82865, Chester N. Weaver Company v. Commissioner of Internal Revenue, contains all facts and records required by the above-mentioned Court to pass upon the questions of law involved in the three said proceedings docketed in said Board of Tax Appeals as Nos. 82865, 82870 and 82871.

6. That the decision of the United States Circuit Court of Appeals for the Ninth Circuit and any further proceedings of the said Board of Tax Appeals and the respondent herein shall be stayed in proceedings Nos. 82870 and 82871 until the decision in proceedings No. 82865 shall have become final in accordance with the provisions of Section 1005 of the Revenue Act of 1926.

7. That upon the final determination, decision and judgment on the appeal of Chester N. Weaver Company v. Commissioner of Internal Revenue (B. T. A. Docket No. 82865) either party to each of the proceedings of Chester N. Weaver v. Commissioner of Internal [51] Revenue (B. T. A. Docket No. 82870) and Elsie S. Weaver (B. T. A. Docket No. 82871) may apply, upon written notice to the other party, upon this stipulation, and upon a certified copy of the decision, order, or judgment of the United States Circuit Court of Appeals for the Ninth Circuit in the Appeal of Chester N. Weaver Company v. Commissioner of Internal Revenue for an order directing judgment to be entered in each of said proceedings (B. T. A.

Docket Nos. 82870 and 82871) in accordance with the final decision, order, or judgment in said appeal of Chester N. Weaver Company v. Commissioner of Internal Revenue.

Dated, May 17th, 1937.

(Signed) ADOLPHUS E. GRAUPNER
(Signed) ARTHUR E. COOLEY
MORRISON SHAFROTH
Chief Counsel
Bureau of Internal Revenue.
Counsel for Respondent. [52]

ORDER

Upon reading the foregoing stipulation and on motion on behalf of the parties thereto

It Is Hereby Ordered that the procedure stipulated by and between the parties to the above entitled proceeding shall be adopted and that the Clerk of this Court, the Clerk of the United States Board of Tax Appeals, Appellants and the Respondent shall act and proceed in accordance therewith.

Dated: May 17th, 1937.

CURTIS D. WILBUR
Senior Judge of the United States Circuit Court of Appeals for the Ninth Circuit.

[Endorsed]: U.S.B.T.A. Filed May 24, 1937. [53]

[Title of Court and Cause.]

PRAECIPE FOR RECORD

To the Clerk of the United States Board of Tax Appeals:

You are hereby requested to prepare and certify and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, with reference to the petitioner for review heretofore filed by the petitioner in the above-entitled proceeding a transcript of the record in the above cause, prepared and transmitted as required by law and by the rules of said Court, and to include in said transcript of record the following documents or certified copies thereof, to-wit:

1. The docket entries of all proceedings had before the United States Board of Tax Appeals;

2. Pleadings before the said Board of Tax Appeals as follows:

(a) Petition for redetermination, and [54]

(b) Answer of the respondent;

3. Minute order of said Board consolidating the above entitled proceeding for hearing and decision with those of Chester N. Weaver, Docket No. 82870, and Elsie S. Weaver, Docket No. 82871;

4. The findings of fact and opinion of said Board;

5. The decision of said Board;

6. The petition for review and assignment of errors filed by the petitioner in the above-entitled proceeding:

7. The stipulation of facts filed with said Board in the above entitled proceeding and on which the cause was tried;

8. The stipulation and order for consolidation on review of the above-entitled proceeding with the said proceedings of Chester N. Weaver and Elsie S. Weaver dated May 17, 1937;

9. This Praecipe.

ADOLPHUS E. GRAUPNER
ARTHUR E. COOLEY
Attorneys for Petitioner

[Endorsed]: U.S.B.T.A. Filed May 24, 1937. [55]

[Title of Court and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 55, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 26th day of May, 1937.

[Seal] B. D. GAMBLE
Clerk, United States Board of Tax Appeals.

[Endorsed]: No. 8572. United States Circuit Court of Appeals for the Ninth Circuit. Chester N. Weaver Company, a corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review a Decision of the United States Board of Tax Appeals.

Filed June 7, 1937.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

No. 8572

CHESTER N. WEAVER COMPANY, A CORPORATION, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Upon Petition to Review a Decision of the United States Board of Tax Appeals

Proceedings had in the United States Circuit Court of Appeals for the Ninth Circuit.

United States Circuit Court of Appeals for the Ninth Circuit

Excerpt from Proceedings of Wednesday, March 16, 1938

Before GARRECHT, HANEY, and STEPHENS, Circuit Judges

No. 8572

Order of submission

Ordered above cause argued by Mr. Adolphus E. Grauper, counsel for petitioner, and by Mr. M. Leo Looney, Special Assistant to the Attorney General, counsel for respondent, and submitted to the court for consideration and decision.

United States Circuit Court of Appeals for the Ninth Circuit

Excerpt from Proceedings of Thursday, June 2, 1938

Before GARRECHT, HANEY, and STEPHENS, Circuit Judges

No. 8572

Order directing filing of opinion and dissenting opinion, and filing and recording of judgment

By direction of the Court, ordered that the typewritten opinion and dissenting opinion this day rendered by this court in above cause be forthwith filed by the clerk, and that a judgment be filed and recorded in the minutes of this court in accordance with the majority opinion rendered.

United States Circuit Court of Appeals for the Ninth Circuit

No. 8572

CHESTER N. WEAVER COMPANY, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Upon Petition to Review a Decision of the United States Board of Tax Appeals.

This Cause came on to be heard on the Transcript of the Record from the United States Board of Tax Appeals and was duly submitted.

On Consideration Whereof, it is now here ordered and adjudged by this Court that the Decision of the said Board of Tax Appeals in this Cause be, and hereby is, reversed.

[Endorsed:] Judgment. Filed and entered June 2, 1938. Paul P. O'Brien, Clerk.

United States Circuit Court of Appeals for the Ninth Circuit

(Title of cause and number)

Certificate of Clerk, U. S. Circuit Court of Appeals for the Ninth Circuit, to record certified under rule 38 of the Revised Rules of the Supreme Court of the United States

I, Paul P. O'Brien, as Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, do hereby certify the foregoing eighty (80) pages, numbered from and including 1 to and including 80, to be a full, true, and correct copy of the entire record of the above-entitled case in the said Circuit Court of Appeals, made pursuant to request of Mr. N. A. Townsend, Acting Solicitor General of the United States, counsel for the respondent, and certified under Rule 38 of the Revised Rules of the Supreme Court of the United States, as the originals thereof remain on file and appear of record in my office.

Attest my hand and the seal of the said the United States Circuit Court of Appeals for the Ninth Circuit, at the City of San Francisco, in the State of California, this 1st day of August A. D. 1938.

[SEAL] (Sgd.) PAUL P. O'BRIEN, *Clerk.*

In the United States Circuit Court of Appeals for the Ninth Circuit

No. 8572. June 2, 1938

CHESTER N. WEAVER COMPANY, A CORPORATION, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Upon Petition to Review a Decision of the United States Board of Tax Appeals

Before GARRECHT, HANEY, and STEPHENS, Circuit Judges

HANEY, Circuit Judge.

Review is sought of a decision of the Board of Tax Appeals which sustained a determination of respondent that there was a deficiency in the income tax paid by petitioner for the year 1933.

Petitioner, a California corporation, on August 9, 1932, purchased from Jeff R. Townsend Company, Inc., a California corporation, hereinafter referred to as the Townsend company, 1,000 shares of the latter's preferred stock, paying therefor $100 per share. The Townsend company's articles of incorporation provided that in the event of liquidation, its preferred stockholders would be entitled to receive a sum equal to 105 per cent of the par value of the preferred stock before any amount would be distributed to the holders of its common stock.

In 1933, the Townsend company became financially involved and unable to continue its business. On September 17, 1933, in order to dissolve and liquidate, it sold all its assets for $26,280.50, which on the next day was distributed pro rata to its preferred stockholders, who at the same time surrendered their certificates for preferred stock. Petitioner received a liquidating dividend in the sum of $13,140.25.

In its income tax return for the year 1933, petitioner claimed a deduction of $86,859.75 as a loss on such preferred stock, being the difference between the amount paid by petitioner for the stock, and the amount of the liquidating distribution. Respondent disallowed the deduction because "the loss sustained in connection with the stock is held to be from an exchange of stock held less than two years" and petitioner "had no gain from sales or exchanges of assets held less than two years." Respondent relied on Sec. 23 (r) of the Revenue Act of 1932 (47 Stat. 169).

On petition to redetermine the deficiency the Board sustained respondent, holding that "this disposition of the stock, under the provisions of the statute considered above, was a sale or exchange and the deduction of the losses sustained is barred by the provisions of section 23 (r) (1)." Five members of the Board dissented. The instant petition to review the decision of the Board, entered pursuant to its holding, was then filed.

Section 21 of the act provides:

"'Net income' means the gross income computed under section 22, less the deductions allowed by section 23."

Section 22 provides in part:

"(a) 'Gross income' includes * * * income derived from * * * sales, or dealings in property * * *

"(d) Distributions by corporations shall be taxable to the shareholders as provided in section 115."

Section 23 provides in part:

"In computing net income there shall be allowed as deductions: * * *

"(f) Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise * * *

"(r) (1) Losses from sales or exchanges of stocks and bonds * * * which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges * * *"

Section 115 provides in part:

"(c) Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112 * * *"

We think that petitioner is entitled to the deduction by virtue of sections 22 (d), 115 (c), and 112. The amount received by petitioner was a liquidating dividend. Under section 22 (d), that dividend is taxable as provided in section 115 (c). Under the latter section, the gain or loss is to be computed under section 111 but the amount arrived at by the computation shall be recognized to the extent provided in section 112. Under section 112, the entire amount of the loss must be recognized.

Petitioner contends that the deduction is authorized by section 23 (f), and argues that the limitation in section 23 (r) (1) is not applicable. Section 23 (f) is a general statute relating to losses, whereas sections 22 (d), 115 (c), and 112 are special with respect to the particular situation. Where there are two statutes, one being a general statute, and the other being a specific statute, and both cover the same subject matter, the specific statute should control. Therefore, we think section 23 (f) should not be applied.

Respondent contends that section 23 (r) (1) prohibits the deduction. It is asserted, as the Board held, that in effect there was an exchange of the stock for money. Petitioner argues, as the dissenting opinion of the Board members points out, that the legislative history of section 23 (r) (1) was not intended to apply to such a situation as is present here. We think section 23 (r) (1) is not applicable.

First. Section 23 (r) (1) is broader and includes more transactions than sections 22 (d), and 115 (c) and 112. As compared with those sections, it again is general. The specific statute should control rather than the general statute.

Second. By its terms section 23 (r) (1) applies only to "sales or exchanges." We think the liquidating dividend here is neither, within the ordinary and accepted meaning of those terms. A "sale or exchange" implies, we think, that each party to the transaction shall obtain something. We do not believe that the Townsend company received anything. There is no inconsistency with the application of section 115 (c), because it does not say a liquidating distribution is an "exchange," but says it "shall be treated" as such for the purpose of applying sections 111 and 112. It does not say that a liquidating distribution shall be treated as an "exchange" for the purpose of section 23 (r) (1).

Third. Had there been no liquidating dividend on the stock, petitioner could have deducted the entire loss. Reg. 77, Art. 174. (Same rule applies to bonds. Art. 194.) The rule announced by the Board leads to the conclusion that a holder of $100,000 of stock who gets a liquidating dividend of ten cents, cannot deduct his $99,999.90 loss. Such construction should be avoided, we think, on the authority of United States v. Katz, 271 U. S. 354, 357, where it is said:

"All laws are to be given a sensible construction; and a literal application of a statute, which would lead to absurd consequences, should be avoided whenever a reasonable application can be given it, consistent with the legislative purpose * * *"

Fourth. The most that can be said for respondent, is that it is doubtful whether Sections 22 (d), 115 (c), and 112, on the one hand, or section 23 (r) (1) on the other hand is applicable. The rule announced in Gould v. Gould, 245 U. S. 152, 153, is applicable, we think, and is: "In case of doubt they [taxing statutes] are construed most strongly against the Government, and in favor of the citizen." Therefore, section 23 (r) (1) should be construed as not applicable to petitioner.

We believe it is unimportant, whether the "deduction may be taken in the form of a minor or negative item of gross income," as mentioned by the Board, or whether it is taken as an outright deduction.

Decision reversed.

STEPHENS, Circuit Judge, dissenting:

The Chester N. Weaver Company, the petitioner here, is a California corporation. Consolidated on review and dependent on the decision of this court upon this petition are petitions for review brought by Chester N. Weaver and Elsie S. Weaver.

On December 2, 1931, Mr. and Mrs. Weaver purchased 500 shares each of the six per cent cumulative preferred stock of the Jeff R. Townsend Company, hereinafter referred to as the Townsend Com-

pany, paying therefor $500 per share. On August 9, 1932, the Weaver Company acquired from the same corporation 1,000 shares of its preferred stock at the same price per share. The 2,000 shares of preferred stock so purchased constituted all of the preferred stock of the Townsend Company. The common stock belonged to other interests. The articles of incorporation provided that in the event of liquidation the holders of preferred stock should be entitled to receive therefor a sum equal to 105 per cent of the par value thereof before any amount should be distributed to the holders of the common stock.

Early in 1933 the Townsend Company became financially involved and unable to continue business. Its stockholders took the necessary steps to effect its dissolution and liquidation. On or about September 17, 1933, it sold all of its assets to the Weaver Company for $26,780.50. On September 18, 1933, the two Weavers and the Weaver Company, holders of all of the preferred stock of the Townsend Company, surrendered their stock certificates for cancellation and for the purpose of completing liquidation and effecting dissolution of that company. The $26,280.50 received for its assets was distributed in liquidation to the preferred stockholders pro rata. The Weaver Company received $13,140.25; Chester N. Weaver, $6,560.13, and Elsie S. Weaver, $6,570.12.

In their income tax returns for 1933 each of the stockholders deducted as a loss the difference between the amount paid for the preferred stock so surrendered and the amount received in liquidation, and, in determining the deficiencies herein, the Commissioner disallowed the deductions so claimed.

The Board of Tax Appeals held that the deductions were barred by Section 23 (r) (1) of the Revenue Act of 1932, c. 209, 47 Stat. 169, and approved the Commissioner's determination. Accordingly it decided that the deficiency due from the Weaver Company amounted to $4,323.48; that from Chester N. Weaver, $8,832.43; and that from Elsie N. Weaver, $2,447.84.

Section 23 (r) (1) provides as follows:

"Losses from sales or exchanges of stocks and bonds [as defined in subsection (t) of this section] which are not capital assets [as defined in section 101] shall be allowed only to the extent of the gains from such sales or exchanges [including gains which may be derived by a taxpayer from the retirement of his own obligations]."

Since it is not claimed by the petitioner that the surrendered stock was a capital asset or that it has non-capital gains which might offset the loss here claimed, the only question presented is whether the petitioner's act of surrendering its stock in the Townsend Company and that company's act of paying the petitioner $13,140.25 for the stock which was in complete liquidation of the company, constituted a sale or exchange of stock within the meaning of Section 23 (r) (1). If it did the decision of the Board disallowing the claimed deduction was proper.

In order to decide the question before us, it seems advisable to relate section 23 (r) to other applicable sections in the framework

of the Revenue Act. Sections 11, 12, and 13 of the Revenue Act of 1932 provide for a yearly tax upon the net income of every individual and every corporation. Section 21 provides that:

"'Net income' means the gross income computed under section 22, less the deductions allowed by section 23."

It is evident, then, that in claiming the right to take a deduction it is necessary to show that it is authorized by section 23. New Colonial Co. v. Helvering, 292 U. S. 435, 440.

Among other allowable deductions enumerated in section 23 is that set out in subsection (f):

"Losses by Corporations.—Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise."

It is under authority of last-quoted subsection that petitioner claims the right to deduct the difference between the amount paid for the Townsend Company stock and the amount distributed to it as a stockholder on liquidation of that corporation.[1]

It is to be noted that section 23 (f) is self-limited by section 23 (r) [which has been quoted above]. The general effect of the two subsections when taken together is that a corporation may deduct all losses it sustains, provided, however, that if a loss results from a sale or exchange of stocks or bonds it may be deducted only to the extent that the corporation has gained from such sales or exchanges.

Petitioner's position is that it suffered a loss on the liquidation of the Townsend Company and that this loss did not result from a sale or exchange of stocks or bonds, and that consequently the whole amount thereof is deductible. One branch of petitioner's argument is founded on quotations from Congressional committee reports. It is asserted that these reports show that Congress did not intend to make liquidation distributions subject to the limitations of section 23 (r). We do not think it is proper to resort to such sources, since, as will be seen, the Act itself provides the solution to the problem without extraneous aid. Moreover, the reports relied on afford, at best, merely negative evidence of the Congressional intent. The fact that the reporting committees have nowhere specifically stated that distributions on liquidation were to be treated as exchanges within the meaning of section 23 (r) is not persuasive that they intended to exclude such transactions from the operation of that section.

A second argument advanced by the taxpayer is that section 22 makes it clear that there is a distinction between a sale or exchange on one hand and a distribution in liquidation on the other. It is pointed out that subsection (d) of section 22 provides that:

"Distributions by corporations shall be taxable to the shareholders as provided in section 115."

[1] Section 23 (e) which applies to individuals, has the same effect, insofar as we are here concerned, as has 23 (f) in the case of corporations.

while in the next subsection (e) it is provided that:

"In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in sections 111, 112, and 113."

It is urged that the differentiation thus made in Section 22 between a corporate distribution and a "sale or other disposition of property" shows that a distribution on liquidation is not a "sale or exchange" within the meaning of section 23 (r). We do not find this argument persuasive—in fact the provisions thus called to our attention are in the last result influential toward a conclusion opposite to that suggested by petitioner. That such is their effect, we think, becomes clear when section 115 [to which section 22 (d) refers] is examined.

Section 115 [which is entitled "Distributions by Corporations" as is section 22 (d)] defines the term "dividend" in subsection (a); and in subsection (b) fixes the source of corporate distributions for the purposes of the Act. Subsection (c) provides in pertinent part:

"Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112."

We believe that the phrasing of this section shows an intent to settle for tax purposes the somewhat anomalous character of a liquidation distribution transaction as a sale or exchange of the stock for the amount distributed. We think this interpretation is borne out when, as directed by section 115 (c), reference is made to section 112, for that section is concerned only with the recognition of gain or loss upon "the sale or exchange of property"—if a distribution in liquidation is not fixed as a "sale or exchange" by section 115 (c) the reference therein to section 112 would be without effect.

It is further significant to note that section 23 (r) first appeared in the Revenue Act of 1932. The Revenue Act of 1928[2] contained subsections (d) and (o) of section 22 and subsection (c) of section 115 in form identical with that in which they appear in the 1932 act. Thus it appears that when subsection (r) of section 23 was enacted, distributions in liquidation had previously been impressed with the character of payments on sale or exchange. The reenactment without change of the sections characterizing liquidation distributions as exchanges, in the Act which first limited the deductibility of losses on stock sales or exchanges, is strongly indicative of the intention of Congress to include within the limitation provisions of section 23 (r) such liquidation transactions.

In addition to petitioner's contentions so far discussed another argument, or an elaboration of that just disposed of, has been advanced. Ingenious though it may be we do not consider it sound.

[2] May 29, 1928, c. 852, section 22, 115, 45 Stat. 797, 822. Substantially identical provisions were also included in the Revenue Acts of 1918, 1924, and 1926.

The elaboration is based upon the reference in section 22 (d) to section 115, which section in turn refers to sections 111 and 112. The substance of this supplemental argument is: under the reference in 115 (c) only subsection (c) of section 111 is applicable since that subsection alone deals with "exchanges," with which character 115 (c) endows distributions in liquidation; that section 111 (c) refers to section 112 for the recognition of loss in the case of an "exchange"; and that section 112 (a) [the only portion of section 112 which is applicable] provides that upon an "exchange" the entire amount of the gain or loss is to be recognized. It is not clear whether petitioner advances the foregoing argument only to bolster the contention that the Revenue Act clearly recognizes a distinction between a "distribution in liquidation" and an "exchange" or whether petitioner is claiming that losses resulting to stockholders from corporate liquidations are to be given effect through section 22 (d) without regard to the provisions of section 23. The latter interpretation was given the argument by the Board.

Since, as we see it, the statutory analysis upon which the argument proceeds is faulty it can be given no weight wherever it is intended to lead.

Section 111 (c), claimed to be the sole provision of section 111 applicable under reference from section 115 (c), does not fix the mode of determination of gain or loss [for which purpose 115 (c) refers to 111] but merely refers to section 112 for the provisions governing recognition of the loss determined under other of its own provisions. Unless then we assume that the law-making body performed a useless act when it enacted in section 115 (c) a reference to section 111, we are bound to give application to other portions of section 111 than subsection (c) thereof for 115 (c) itself refers to section 112 for recognition of loss. Again, if petitioner's argument were to be accepted the result would be that though 115 (c) distinguishes between "determination" and "recognition" of gain or loss by reference to sections 111 and 112, respectively, the net effect of the references would be the "recognition" of a gain or loss nowhere "determined." Moreover, when section 111 is read as a whole, the expression "sale or other disposition of property" used in subsections (a) and (b) thereof is seen to have been intended to cover an "exchange" for subsection (c) thereof refers to section 112 only in those instances in which there has been a determination "under this section [section 111]" of the extent of gain or loss on "a sale or exchange." There could be no determination of loss on an "exchange" under section 111 unless the phrase "other disposition of property" contained in that section is inclusive of "exchange."

Moreover, if losses on liquidation distributions are to be governed by the provisions of section 22 (d), 115 (c), 111, and 112 without regard to section 23, logic would lead to the conclusion that section 23 (r) is in no case to be given any effect. This is true because both in the case of a "distribution by a corporation" [22 (d)] and

in the case of a "sale or other disposition of property" [22 (e)] the ultimate reference is to section 111 for "Determination," and to section 112 for "Recognition" of gain or loss. If the provision of section 112 to the effect that the entire amount of gain or loss (determined under section 111) shall be "recognized" means in the case of liquidation that such loss may be deducted independent of the provisions of section 23, the same result must follow in the case of a sale of stock. And if it does follow, then section 23 (r) can be given no effect or operation. By the same token the references made in subsections (e) and (f) of section 23 to "the limitations provided in subsection (r)" would be purposeless, for the transactions limited by "subsection (r)" do not, under this view, come within the purview of 23 (e) or (f).

I conclude that the separate provision in section 22 as to distributions by corporations on one hand and sales or other dispositions of property on the other hand does not make a distinction between a distribution in liquidation and a sale or exchange such as to prevent the application of section 23 (r). On the contrary the ultimate effect of these provisions is to make it clear that such transactions are "exchanges" within the meaning of section 23 (r) and therefore subject to the limitations therein provided. The rule is long-established that the intention of the lawmaker is to be deduced from a view of every material part of a statute. Hellmich v. Hellman, 276 U. S. 233, 237. Congress having classified a transaction involving a distribution in liquidation as an exchange such classification requires it to be treated as coming within any provisions pertaining to exchanges.

It has previously been held that the provision of section 115 (c) that amounts distributed in liquidation "shall be treated as in full payment in exchange for the stock" characterizes such transactions as "exchanges" for income tax purposes. In White v. U. S. (Ct. of Clms. 1937), 21 F. Supp. 361, it was held that an amount received by a holder of preferred shares on partial liquidation of a corporation was properly treated as a "capital" rather than an "ordinary" loss, the court stating that the provisions of section 115 (c) "make a liquidating dividend have the same effect as a sale or exchange of property" and that consequently the distribution in question was a "deductible loss resulting from the sale or exchange of capital assets" within the meaning of section 101 (c) (2). See also, Eckols v. Commissioner (C. C. A. 8, 1932), 61 Fed. (2d) 191; Childs v. Commissioner, 35 B. T. A. 1125 (1937); Reg. 77, Art. 625.

The argument that section 23 (r) is not here applicable because it is broader and includes more transactions than sections 22 (d), 115 (c), and 112 and consequently should not control the last named sections, has validity only if the so-called "specific" statutes are in conflict with the so-called "broader" statutes. The statutes are not in conflict unless it is thought that sections 22 (d), 115 (c), and 112 in and of themselves allow a loss deduction by way of a minus item

of gross income. I have above suggested my reasons for thinking that they do not.

While it is true that the general rule is that acts levying taxes are, in case of doubt, to be construed in favor of the citizen, in my opinion the more specific rule applicable here is that deductions, like exemptions, are privileges, and a person claiming a deduction must point to an applicable statute and show that he comes within its terms. New Colonial v. Helvering, 292 U. S. 435, and cases cited; see also, Paul & Mertons, Law of Federal Income Taxation, Vol. I, section 330 (1937 Cum. Supp.).

The suggestion that in a stated hypothetical case a harsh result will follow from the conclusion that a distribution in liquidation is an exchange within the intendment of section 23 (r) is, I think, answered by the following quotation from Helvering v. Twin Bell Syndicate, 293 U. S. 312, 321:

"The respondent insists that, so applied, the sections may work unjust and unequal results, but it is to be remarked that this is likely to be so wherever a rule of thumb is applied without a detailed examination of the facts affecting each taxpayer. No doubt as the petitioner points out, equally illogical results might ensue from the application of the section, as the respondent construes it."

See also, Eckols v. Commissioner, supra.

I am of the opinion that the decision should be affirmed.

[Endorsed:] Opinion and dissenting opinion. Filed June 2, 1938. Paul P. O'Brien, Clerk.

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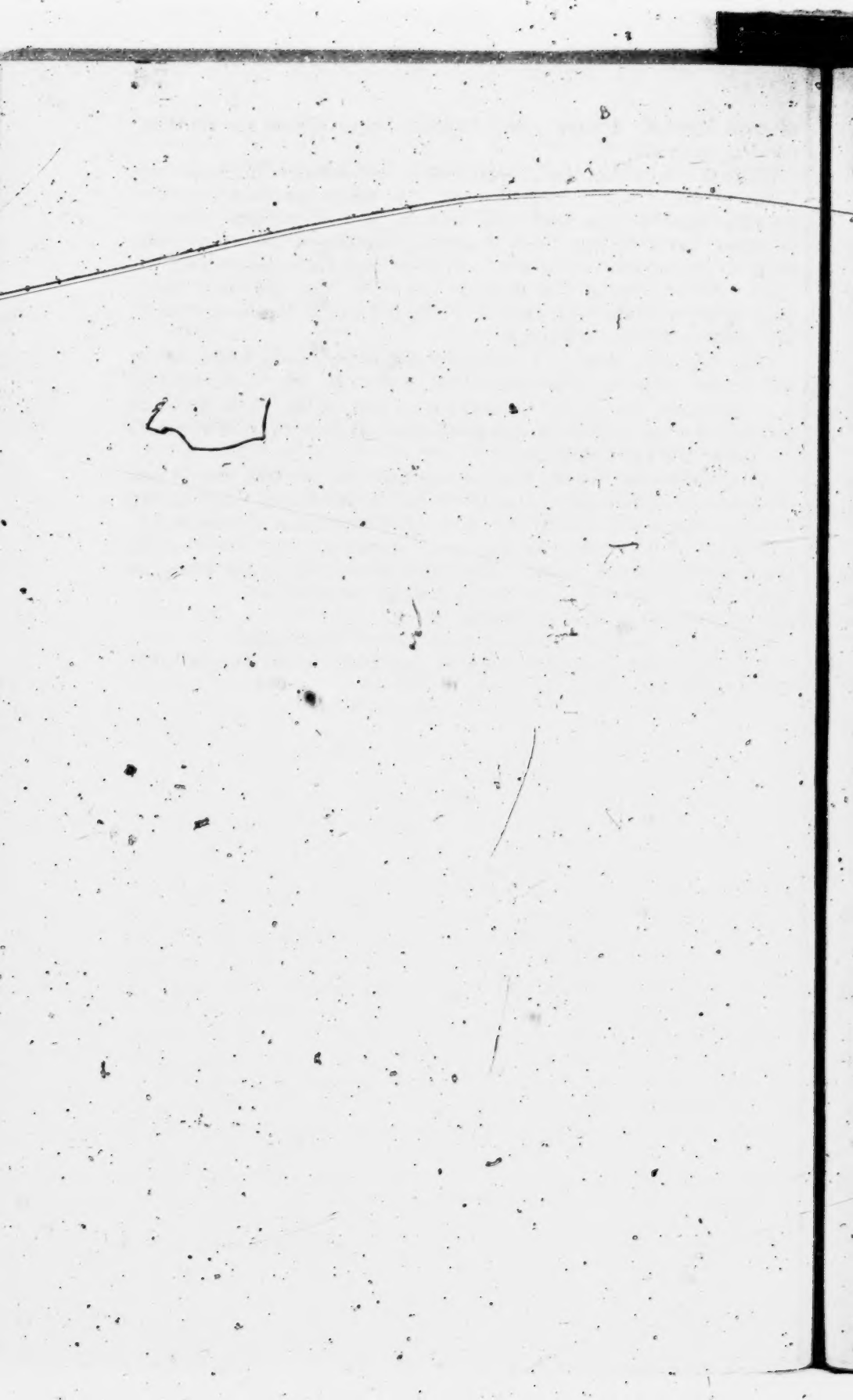

Order allowing certiorari

Filed October 10, 1938

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Ninth Circuit is granted, and the case is assigned for argument immediately following Nos. 96 and 97.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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